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## ALEC POLICY FORUM

# Bypassing Expert Regulation through False Claims Litigation

BY ANTONIO DIAS, ANDERSON BAILEY, AND WILLIAM SEITZ

State false claim act laws and provisions for *qui tam* lawsuits are rapidly expanding and drawing the attention of a number of legislators. Of particular concern are efforts by claimants to circumvent the regulatory process by using these laws to chase conduct that fully informed regulators have not chosen to pursue.

False claim laws were designed to address fraud against the government. The federal *False Claims Act* (FCA) prohibits making "a false or fraudulent claim for payment" to the government and permits private individuals, known as *qui tam* relators, to bring suits on the government's behalf in return for a percentage of the recovery. First enacted to police fraud among contractors during the Civil War, the statute lay relatively dormant for more than a century. But in 1986, Congress amended the law to allow treble damages and penalties, increase the relators potential share, and shift counsel fees onto unsuccessful defendants. Over time, these laws relieved plaintiffs of the burden to prove true fraud, for example by expressly providing that the relator need not prove any intent to defraud by defendant or any detrimental reliance by the government. The federal government also began encouraging states to enact their own versions of the FCA, and 29 states now have false claims laws, many of which mirror the damages and relator provisions in their federal counterpart.

*Qui tam* litigation has exploded as a result, with more than 600 new cases reported in 2011, compared to only 30 in 1987. The plethora of filings should not be mistaken for the merit of them, however. According to the Department of Justice, it intervenes in fewer than 25 percent of FCA cases, and most relators dismiss their claims when advised the government will not join their suit. Moreover, when the government does intervene, defense attorneys often encourage their clients to settle regardless of whether they've committed any wrongdoing as this is the surest way to protect against the draconian threat of treble damages and penalties.

The result is a windfall to relators and their counsel. Over the first decade of the 2000s, the combined relators share from all FCA cases averaged over $250 million per year, while this number exceeded $532 million in 2011 alone. When the government chooses to intervene, the chance of recovery significantly increases. The government carries a heavy hammer when joining this type of litigation—a tool that should be used wisely.

Lured by the prospect of a lucrative settlement, *qui tam* plaintiffs and their attorneys are lobbying for changes that will facilitate even greater recovery. They are also aggressively testing the boundaries of false claims liability. Through lawsuits based on theories of "legal falsity" and "implied false certification," *qui tam* plaintiffs are using state and federal false claims laws not as a way of redressing fraud, but as a way of improperly policing compliance with government regulations—often in a manner that conflicts with the actions of the agencies that promulgate, interpret, and enforce those regulations.

A recently filed *qui tam* lawsuit in Pennsylvania exemplifies this potential for abuse. In *Washington v. Education Management Corporation* (EDMC), the federal government and some states have joined a *qui tam* lawsuit in which relators allege that EDMC violated a Safe Harbor provision in Department of Education (DOE) regulations governing the compensation of admissions representatives at colleges and universities run by EDMC.

Congress delegated to the DOE the authority to enforce these regulations, and that agency has an established procedure for correcting violations. However, despite knowing for years about EDMC's compensation practices, the DOE has taken no action against EDMC, but has at all times certified EDMC's schools as eligible to receive federal funding, and continues to disburse educational loans and grants to EDMC's students.

Nevertheless, *qui tam* plaintiffs and the government are using the FCA to claim that EDMC and its schools were actually in violation of the recruiter-compensation provision, and ineligible for funding. Arguing that each funding application for an EDMC student constituted an "implied certification" of compliance with the DOE regulation, plaintiffs assert that those certifications were false within the meaning of the FCA, and that EDMC's schools should be liable for treble damages and penalties based on hundreds of thousands of individual applications.

Skepticism toward these claims is beginning to grow among courts, and as state false claims act legislative initiatives are evaluated, consideration should be given to whether profit-minded plaintiffs and their attorneys should be allowed to use *qui tam* lawsuits to swallow the regulatory process. Plaintiffs are second-guessing regulators, creating discord in regulatory regimes that industry is entitled to rely upon, and targeting defendants with costly and potentially high-damage litigation.

But false claims lawsuits are not appropriate substitutes for the expertise and discretion of administrative agencies. The power of private plaintiffs to allege and pursue FCA claims in the name of the government should be narrowly defined and permitted only after exercising the appropriate due diligence.

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# ALEC's *Jury Patriotism Act*

*Reducing Hardship for Thousands of Jurors and Ensuring Representative Juries on Complex Cases*

BY CARY SILVERMAN

Jury service is an important obligation of citizenship that is vital to both the civil and criminal justice systems.

Not only is it a civic duty for individuals to serve, litigants depend on a representative jury for a fair trial. When entire segments of the population are missing from the jury pool, excluding their perspectives from decision making, there is a greater chance of a "runaway" jury that reaches an extraordinary verdict.

ALEC has made a significant contribution to creating more flexible, less burdensome jury service systems that have allowed a broader range of citizens to serve through its model *Jury Patriotism Act* (JPA). In strained economic times, those who are summoned are often forced to make a choice between paying their bills and reporting for jury service for several days. In this environment, the JPA takes on special importance as a critical tool for preserving representative juries and maintaining confidence in state judicial systems.

## ENACTMENT IN THE STATES

Since its development, more than a dozen states have enacted all or portions of the JPA, which incorporates the best practices of the states as recognized by the National Center for State Courts and the American Bar Association. The JPA makes jury service less burdensome by providing summoned jurors with a hassle-free system for rescheduling jury service, ensuring that citizens are not repeatedly called to serve, and limiting the length of service to no more than one day if not selected to serve on a jury or the duration of one trial. Some courts have adopted reforms included in the JPA on their own initiative. For instance, last November, Gwinnett County, Georgia began a pilot project of the one-day/one-trial system that has both made jury service more convenient for citizens and is projected to reduce court costs by $100,000 annually through its increased efficiency.

Given the increased flexibility of jury service, the JPA closely defines the grounds for obtaining a full excusal from jury service rather than a postponement. It also eliminates outdated exemptions that permitted individuals in certain occupations to avoid jury service. The goal is to ensure that everyone can and does serve.

## REDUCING THE BURDEN OF SERVING ON LENGTHY TRIALS

The most innovative element of the JPA is its Lengthy Trial Fund (LTF), which has allowed thousands of citizens in Arizona and Oklahoma to serve as jurors who judges might otherwise have felt compelled to excuse for financial hardship. Reports from around the country repeatedly show the difficulty in finding jurors who are able to serve on lengthy trials. In such cases the stakes are often quite high. In criminal cases, prosecutors seek justice for horrible crimes, while defendants may face life imprisonment or the death penalty. In civil litigation, personal injury attorneys may seek millions in compensation, plus punitive damages for their clients. Such a verdict can push a business defendant into bankruptcy and threaten the jobs of its employees. Yet in these types of cases, entire groups of people cannot serve on juries. Those who are self-employed, independent contractors, hourly wage earners, or owners or employees of small businesses—taxi drivers, plumbers, accountants, shopkeepers—are unlikely to participate in jury service without incurring extreme and unfair financial hardship.

Take for example the recent Casey Anthony trial that captivated the media in 2011. A Florida court summoned more than 400 people for jury service; as it anticipated the need to excuse many people on what was expected to be a two-month murder trial. During the first day of jury selection, a man asked to be excused because he would not receive compensation from his employer during jury service. Orange-Osceola Chief Judge Belvin Perry asked him what would be the impact if he was selected to serve and received only the $30 per diem provided to Floridians who serve as jurors on trials lasting more than three days. "I'd probably be in bankruptcy by the end of 12 weeks," the man said. A second juror who would not be paid during jury service asked to be excused. She was afraid that she would lose her car and be evicted without her income. Judge Perry did not excuse the first juror for hardship, but let the second go home.

Their concerns are typical. In most states, jurors receive no more than a $10 to $30 per diem for their service. "Most people can't live on $10 a day for a half-month," said Paula Hannaford-Agor, Director of the Center for Jury Studies. "It's not going to buy their groceries. It's not going to pay the rent. It's not going to pay the American Express bill when it comes due." Several states increase the per diem to around $40 after the third day of service. New Mexico pays its jurors minimum wage. Nevertheless, when a trial extends over several weeks or months, a juror who is not receiving his or her usual income will suffer a tremendous hardship if not excused.

To address financial hardship issues that undermine citizen participation, the model act's LTF makes supplemental compensation available to jurors in this position. As suggested by the model act, jurors who serve on trials lasting longer than three days can request supplemental compensation of up to $100 if they would otherwise be excused from service due to financial hardship. In the rare case that a trial lasts ten days or more, any juror who is not fully compensated by their employer during jury service or who does not receive their usual income would be eligible to receive supplemental compensation of up to $300 per day from the fund. Obviously, in times of tight state budgets, a substantial increase in juror compensation funded by taxpayers is not in the cards. The JPA addresses this concern by spreading the costs of LTF on those who use the courts by placing a nominal fee on the filing of civil cases.

## THE ARIZONA EXPERIENCE

Arizona was the first state to enact legislation based on ALEC's model JPA, including the LTF, in 2003. According to Arizona's Administrative Office of the Courts (AOC), "Jury commissioners throughout the state have reported that the lengthy trial fund is a welcome reform that has allowed a number of citizens to serve on juries who would not have been financially able to serve without reimbursement of lost earnings offered by the fund."

The Arizona LTF provides supplemental compensation to about 1,000 jurors each year. Jurors receive an average of $69 per day in reimbursement based on their lost income, according to the AOC. Where jurors would have otherwise received no more than the $12 per diem provided by the county and mileage, the LTF additionally has provided them with earning replacement that, on average, amounts to $600 on a lengthy trial.

Far from running short of funds, as some had feared, the LTF, which is financed in Arizona through a $15 fee on the filing of civil complaints and answers, has consistently run a surplus. Arizona's Fiscal Year 2013 budget continues to anticipate that court fees collected will more than fully cover juror requests.

As a result, the Arizona Legislature has repeatedly expanded eligibility for compensation from the fund. Under current Arizona law, a juror whose service lasts more than five days may request earnings replacement of up to $300 per day beginning on the fourth day of jury service. The legislature also opted to provide unemployed and retired jurors who serve on juries for more than five days with minimum juror compensation of $40 (the $12 per diem provided by the counties plus $28 from the LTF).

The Arizona Legislature is considering a bill (S.B. 1142) that once again would change the time that jurors on lengthy trials begin receiving earnings replacement from the LTF. Those who serve on a jury for more than five days, with a loss of income would be eligible to receive up to $300 per day in earnings replacement for their entire period of jury service. At the time of this writing, the bill has passed the Arizona Senate with unanimous support and looks likely to be enacted into law.

To find out how the JPA can help improve your state's jury service laws, contact Amy Kjose, Director of ALEC's Civil Justice Task Force.

**CARY SILVERMAN** is an advisor to the Civil Justice Task Force and is Of Counsel with the Public Policy Group at Shook, Hardy & Bacon, LLP.

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# Who Pays When the 'Loser Pays'? Considering Practical Issues, Misperceptions and Options

BY VICTOR E. SCHWARTZ AND CARY SILVERMAN

In recent months, state officials have expressed significant interest in adopting "loser pays" – a system under which the losing party in a lawsuit must pay the opposing party's attorneys' fees and costs. Texas Governor Rick Perry touted his state's enactment of a "loser pay" law on the campaign trail. South Carolina Governor Nikki Haley, in an address at the U.S. Chamber of Commerce's annual Tort Reform Summit, declared loser pays to be among her top civil justice priorities. In 2012, New Hampshire and Tennessee considered forms of loser-pays bills.

A loser-pays system has strong appeal. After all, even when an individual or business "wins" a lawsuit, the cost of defending against a meritless claim can easily rise into the tens or hundreds of thousands of dollars. These expenses, which are typically not recoverable, become a cost of doing business in America—it is part of the "tort tax." Theoretically, a loser-pays law should deter lawyers from filing weak claims. Some respected scholars and advocacy groups strongly support a loser-pays system.[1] There are questions, however, as to whether the pure form of a loser-pays law, known as the "English Rule" achieves this result in practice.

Given the rising interest in enacting loser-pays laws, it is important to consider how these laws might work in court, some common misperceptions, and legislative options. Some have expressed concern that a loser-pays system will be unevenly applied against defendants—adding attorneys' fees on top of liability that many already generally view as excessive. Legislation strengthening rules against frivolous claims and vexatious litigants may provide a better option.

## DOES "LOSER PAYS" MEAN "DEFENDANT PAYS"?

A recent panel discussion hosted by the American Tort Reform Association (ATRA) featured three practitioners with a combined 80 years of trial experience defending manufacturers in product liability lawsuits. They shared their common view that while a loser-pays law may explicitly state that it applies to both sides in litigation, in the courtroom judges would apply it unequally to impose additional liability on a losing defendant. On the other hand, the participating litigators believed that plaintiffs who lose meritless lawsuits would be let off the hook. There are two reasons why: resources and judicial discretion.

Plaintiffs in personal injury cases typically hire lawyers on a contingency-fee basis because they do not have money available to pay an attorney's hourly rates. Should a prevailing defendant attempt to collect attorney's fees from a losing plaintiff, it would often find that the plaintiff is "judgment proof" and has no money to pay. In these situations, seeking recovery of attorneys' fees would be spending more money to chase money that does not exist.

In addition, a loser-pays law will likely provide some discretion to judges as to when to impose attorneys' fees. When an individual plaintiff loses after battling a "deep-pocket" defendant, sympathetic judges are likely to relieve plaintiffs of their obligation to pay the significant cost of a law firm's hourly rates to defend against the claim. In contrast, a plaintiff who prevails when suing a business will likely receive the entirety of his or her costs and fees.

## THREE COMMON MISPERCEPTIONS

**1. Loser Pays Works in Other Countries, so it Would Work Here.**

Although some countries use a loser-pays system, there are significant differences between their legal systems and insurance environments and our own. It should also not be overlooked that loser-pays systems come with their own exceptions, challenges, and flaws.

Outside the United States, legal systems do not widely use (or permit) contingency-fee agreements. Since personal injury lawyers in the U.S. stand to go uncompensated if their client loses a case, they have a disincentive to bring cases with little likelihood of recovery that is not present where they are paid an hourly fee. For that reason, arguably, there is less need for a loser-pays system here than in countries where contingency-fee agreements are not commonly used.

Individuals in countries such as England and Canada that have a loser-pays system, have insurance that covers them should they bring and lose a lawsuit. While an insurance market could develop in the United States to cover attorney's fees incurred as a result of losing litigation should a state enact a loser-pays law, such a concept could face resistance. It would inject insurers into decisions as whether or not to bring claims and possibly other litigation choices. It is also important to recognize that there are exceptions to loser pays in countries that follow this system. For instance, in Britain, plaintiffs whose cases are brought through legal aid are not required to pay the prevailing party's attorneys' fees.

While loser pays might tempt a plaintiff (or his or her lawyer) to think twice before bringing a claim that clearly lacks merit, some observers of the English system point out that loser pays encourage plaintiffs to bring strong cases involving trivial amounts.[2] By eliminating the expense of the litigation from the plaintiffs' attorneys' lawsuit-bringing calculus, nuisance claims suddenly become highly profitable. Attorneys' fees in such cases can dwarf a client's recovery. We already see this occur in the American civil justice system where consumer protection statutes- in California and elsewhere- that authorize a prevailing plaintiff to recover attorneys' fees have led to the development of a cottage industry for lawyers specializing in suing small restaurants and shops for technical violations of disabled-access laws.[3]

Administration of a loser-pays system also has its own significant challenges, such as determining who is a "prevailing" party. It is common for lawsuits to include several claims. If five of a plaintiff's six claims for relief are dismissed, but a single claim results in a plaintiffs' verdict, is that plaintiff entitled to recover all of his or her attorneys' fees? What if a jury reaches a plaintiffs' verdict but awards only nominal damages or a tiny fraction of what the plaintiff sought? A defendant may consider the result a victory, but find itself subject to paying attorneys' fees and costs. Such circumstances are likely to result in additional litigation and fee disputes.

**2. Alaska Follows Loser Pays.**

Alaska is considered the only state that follows loser pays, but it actually follows a limited version of the system that permits only modest recovery of fees and is riddled with exceptions. Consider, for example, that last November, a jury in a small Alaska town rendered a unanimous verdict for Philip Morris in the first wrongful death case challenging cigarettes as defective to go to trial in the state. One would not expect the judge to order the plaintiff, Dolores Hunter, who lost her husband to cancer, to pay Philip Morris's legal fees. She was not required to do so. The same can be expected in most other cases in which a person claims that the actions of a major employer caused a physical injury or death.

Under Alaska law, a prevailing party may seek a relatively small portion of his or her attorneys' fees ranging from one percent to thirty percent depending on whether the case was contested or uncontested, resolved with or without a trial, and on the amount of the judgment.[4] But Alaska law provides the judge with ten potential reasons to depart from this schedule. Among these reasons is "the extent to which a given fee award may be so onerous to the non-prevailing party that it would deter similarly situated litigants from the voluntary use of the courts." This factor disfavors imposing fees on individual plaintiffs who sue businesses. Another factor is "the extent to which the fees incurred by the prevailing party suggest that they had been influenced by considerations apart from the case at bar, such as a desire to discourage claims by others against the prevailing party or its insurer." This factor counsels against awarding defense costs to a business that has made the strategic decision to vigorously fight each case to discourage plaintiffs' lawyers, who might smell easy money from piling on more claims.

Despite the law's 10 exceptions, the Alaska Supreme Court developed one more—a broad "public interest" exception that favored plaintiffs.[5] "The exception the court created meant that if an environmental group sued to stop a development and lost, it did not have to pay the costs incurred by the other side," noted John Harris, the Speaker of the Alaska House of Representatives, "And, by the way, if the group won on any part of its lawsuit—no matter how small or technical—it would be reimbursed 100 percent of its attorneys fees."[6] The Alaska Legislature found that this exception resulted in "unequal positions in litigation," and after three decades of use, eliminated it in 2003.[7] While the Alaska Supreme Court permitted the legislature's intervention, the court pointed out that the final exception to the state's loser-pays rule, a catchall that allows the court to reduce or not award attorneys' fees due to "other equitable factors deemed relevant," still provided judges with significant discretion not to award fees on a case-by-case basis.[8]

Given the Alaska law's modest right to reimbursement and significant judicial discretion, it is not surprising that an empirical study of the law conducted by the Alaska Judicial Council concluded that loser pays "seldom plays a significant role in civil litigation."[9] Courts awarded fees in only about 10 percent of cases, because many were settled, this resulted in verdicts where neither party prevailed or both parties prevailed in some respect, or a contract or other statute governed the fee award. The three quarters of fee awards were for less than $5,000. In more than half the cases in which the court awarded attorneys' fees, the prevailing party did not pay because the losing party was judgment proof or declared bankruptcy, or because the prevailing party waived fees as part of a post-judgment settlement. Just one in three litigators surveyed could recall a case in which the loser-pays rule played a part in a client's decision to file a lawsuit or to settle a case. The Judicial Council observed that the rule did not seem to have an impact on the filing of frivolous claims, while recognizing that it is difficult to measure such an impact. In fact, plaintiffs' lawyers were among the groups expressing the greatest support for the loser-pays law. More than two-thirds of plaintiffs' lawyers surveyed expressed the view that loser pays worked to their advantage more often than not.

**3. Texas Adopted "Loser Pays."**

While many refer to legislation enacted in Texas in 2011 as "loser pays," the new law is actually very different than the "English rule."[10]

The Texas law has two components. The first part directs the state's Supreme Court to develop a system for dismissing claims at an early stage. Texas was the only state without such a mechanism. Under the new law, the prevailing party on a motion to dismiss is entitled to its attorneys' fees. Courts are very reluctant to grant motions to dismiss, which come soon after filing and before a party has had an opportunity to gain evidence through discovery. Nevertheless, defendants often make such a motion when the legal grounds for a claim are questionable. If adopted elsewhere, legislation based on this provision of Texas law is likely to discourage defendants from seeking early dismissal of weak cases because, unless they fully prevail, defendants would then have to pay the plaintiff's attorneys' fees for responding to the motion. Instead, defendants will wait until later in the case and make what is known as a motion for summary judgment after incurring significant expense in the discovery process.

The second component of the new Texas law makes minor modifications to what is known as an "offer of judgment" rule. This is a relatively common mechanism available in federal and many state courts in which a plaintiff is required to pay certain court costs when he or she previously rejected a settlement offered by the defendant and a trial ultimately resulted in a verdict that was significantly less favorable than the settlement offer.[11] Such laws typically provide only nominal reimbursement of court expenses, which may be less than the cost of seeking such recovery. While the Texas statute provides for substantially greater reimbursement of costs than permitted in federal and other state courts, there are various reasons why this system is rarely used and poses a significant risk for defendants.[12] It is not a very effective mechanism for discouraging meritless lawsuits, and ultimately, it penalizes a party that exercised its right to have the dispute decided in court rather than settle.

## OPTIONS FOR DEVELOPING A "LOSER PAYS" SYSTEM

While a loser-pays system similar to the English Rule may not be effective in the United States, legislators have other tools available to them. When legislators discuss the need for loser pays, the phrase is often followed by "…for frivolous lawsuits." State legislators might therefore best focus their interest in loser pays by supporting legislation that requires those who bring frivolous lawsuits to pay the attorneys' fees and expenses of those who are on the receiving side of such lawsuits.

There is a significant difference between a loser-pays rule that requires a party that brought a viable claim but ultimately did not meet the burden of proof set by law to pay an opponent's attorneys' fees, and one that imposes such costs on those who bring frivolous claims. A "frivolous claim" is typically defined as one that (1) is presented for an improper purpose, such as harassment; (2) is not supported by existing law or a legitimate argument for extending, modifying, or reversing existing law or for establishing new law; or (3) is not supported by the facts and is unlikely to have evidentiary support after a reasonable opportunity for further investigation or discovery.

The need for such reform is greatest in states that follow the approaches used in states that follow the approach currently used in federal courts (known as "Rule 11"). In 1993, the federal judiciary amended the federal rule rendering it, in the words of Justices Scalia and Thomas, "toothless" and allowing "parties . . . to file thoughtless, reckless, and harassing pleadings, secure in the knowledge that they have nothing to lose."[13] In federal courts, an individual or business that is hit with a frivolous claim must draft a motion for sanctions, provide an advance copy to the plaintiffs' attorney, and give him or her 21 days to withdraw the lawsuit and walk away Scott free. If the plaintiff chooses to proceed with the lawsuit, then the defendant still has little likelihood of recovering his costs. Even if a court finds the lawsuit frivolous, the judge has complete discretion as to whether to sanction such conduct. When the judge finds sanctions are warranted, the rule limits any monetary sanction to the amount needed to discourage such claims. Rule 11 awards are not permitted to be used for the purpose of compensating the victim of the frivolous lawsuit. In fact, the court could decide to impose a fine payable into the court, rather than fees to the injured party.

Legislators might consider adopting a law similar to the federal rule that was in place between 1983 and 1993. About a third of the states apply this version of the rule, which does not include the "21-day safe harbor," provides for mandatory sanctions if a judge finds a case is frivolous, and recognizes that sanctions can serve the legitimate function of compensating a wrongly-sued party for its losses in defending itself.

A second option is to consider approaches adopted in states such as Florida, Georgia, Michigan, or Nebraska that generally requires courts to award a prevailing party its reasonable attorneys' fees and costs when the court finds a lawsuit was frivolous.[14] Wisconsin is the most recent state to take such action by providing a more limited "safe harbor" than the federal rule, and permitting use of sanctions to reimburse victims of frivolous lawsuits.[15]

Legislation introduced in Indiana in the 2011 session provides a third approach. The Indiana bill would have required courts, at the conclusion of every case, to evaluate whether the losing party (1) brought the action or defense on a claim or defense that is frivolous, unreasonable, or groundless; (2) continued to litigate the action or defense after the party's claim or defense clearly became frivolous, unreasonable, or groundless; or (3) litigated the action in bad faith. If so, then the court would award reasonable attorneys' fees to the prevailing party.[16]

Finally, in addition to strengthening laws against frivolous claims, legislators might consider adopting a "vexatious litigant" law, which typically requires pro-se plaintiffs (individuals who file lawsuits without an attorney) who repeatedly file and lose lawsuits to obtain permission from the court and post security before filing additional litigation. Such laws have been enacted in states such as California, Florida, Hawaii, Ohio, and Texas.

These options are not intended to be exclusive. Legislators should develop alternatives that (1) are fair to both sides; (2) discourages meritless litigation; and (3) are enforceable in practice, not merely in theory.

Some state courts may view any type of loser-pays legislation as intruding on their judicial authority to develop procedural rules. There is a strong argument, however, that such laws are substantive in nature—they do not merely address the timing for, or manner of, filing a document with the court. Rather, such laws address the very substantive matter of when and how a victim of lawsuit abuse can recover a true financial loss. Legislators can appreciate that such measures are firmly within the tradition of protecting the state's citizens from misconduct, and the legislature's prerogative to reduce barriers to economic growth.

**VICTOR E. SCHWARTZ** serves as the private sector co-chair of ALEC's Civil Justice Task Force and as the chair of Shook, Hardy & Bacon's Public Policy Group. He is also on ALEC's Board of Scholars.

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[1]See, e.g., Marie Gryphon, Greater Justice, Lower Cost: How a "Loser Pays" Rule Would Improve the American Legal System, Civil Justice Rep. No. 11 (Manhattan Inst. 2008); Walter Olson & David Bernstein, Loser-Pays: Where Next?, 55 Md. L. Rev. 1161 (1996).

[2]See Herbert M. Kritzer, "Loser Pays" Doesn't, Legal Affairs (Nov. 2005), at http://www.legalaffairs.org/issues/November-December-2005/argument_kritzer_novdec05.msp.

[3]See, e.g., Chuck Poochigian, Using the ADA to Abuse the Legal System, Union Tribune, Apr. 8, 2005; Walter Olson, The ADA Shakedown Racket, City Journal (Winter 2004).

[4]See Alaska Court Rule 82.

[5]See, e.g., Dansereau v. Ulmer; 955 P.2d 916 (Alaska 1998); Southeast Alaska Conservation Council, Inc. v. State, 665 P.2d 554 (Alaska 1983); Thomas v. Bailey, 611 P.2d 536 (Alaska 1977); Gilbert v. State, 526 P.2d 1131 (Alaska 1974).

[6]Rep. John Harris, Loser-Pays in Alaska: The Way it Should Be, PointofLaw.com (July 30, 2007), at http://www.pointoflaw.com/columns/archives/004140.php.

[7]H.B. 145 (Alaska 2003).

[8]See State v. Native Village of Nunapitchuk, 156 P.3d 389, 405 (Alaska 2007).

[9]Alaska Judicial Council, Alaska's English Rule: Attorney's Fee Shifting in Civil Cases (1995).

[10]See H.B. 274, 82nd Leg., Reg. Sess. (Tex. 2011).

[11]The federal offer-of-judgment mechanism, Rule 68 of the Federal Rules of Civil Procedure, was adopted in 1937.

[12]See Michael Logan, Zach Mayer & Aaron Speer, Offer of Settlement in Texas vs. Offer of Judgment in Federal Court, Feb. 2011, at http://www.krcl.net/index.php?src=gendocs&ref=Litigation-Alert%202011%200201.

[13]Amendments to Federal Rules of Civil Procedure and Forms, 146 F.R.D. 401, 507-08 (1993) (Scalia, joined by Thomas, J.J., dissenting).

[14]Fla. Stat. Ann. § 51.105(1); Ga. Code Ann. § 9-15-14; Mich. Comp. Laws § 600.2591; Neb. Rev. Stat. § 25-824(4).

[15]S.B. 1, § 28, Spec. Sess. (Wis. 2011) (to be codified at Wis. Stat. § 895.044).

[16]S.B. 85 (2012) (proposing amendment to Ind. Code § 34-52-1-1).

# Measuring Improvements in the Tort System

*How improving the legal environment in individual states could reduce tort costs and promote business activity and employment*

BY PAUL J. HINTON AND
DAVID L. MCKNIGHT

Most Americans would probably agree that the tort system plays a vital role in providing victim compensation, deterring wrongdoing and delivering justice. Most would probably also agree that the system could work better. But how much scope is there for improvement through incremental reforms? What's at stake for the economy and how can we assess whether progress is being made?

There is a shortage of reliable measures of tort system performance upon which to base an answer to such questions. Surveys are commonly used to rank state tort systems along various dimensions; however, these rankings generally do not provide objective economic measures. Towers Watson's annual study of tort costs provides an estimate of the total cost of the US tort system, consisting of litigation costs, settlements and awards, but it provides no estimates at the state level.

We completed a research project in October for the U.S. Chamber Institute for Legal Reform ("ILR") in which we developed a metric for measuring tort system costs in each state that may help. It uses an econometric analysis to separate out the effects of the legal environment on costs and uses the least costly states as performance benchmarks. The complete study can be found on the ILR website at www.instituteforlegalreform.com.

Our study reveals that costs attributable to the legal environment vary by 26 percent between the states with the least costly and most costly legal environments. This means that improvements in the legal environment that achieve the performance already seen in the least costly states would save up to 26 percent in tort costs before considering whether even greater improvements might be possible.

Of course, the performance of the tort system has several dimensions: outcomes in terms of compensation, deterrence and justice; cost efficiency; and the extent of unintended economic side effects of litigation. Our analysis measures the costs attributable to characteristics of the legal environment in each state and the potential economic benefits of improvements, but not outcomes. Under the assumption that states with less costly legal environments do not have worse outcomes, our analysis provides a metric of cost efficiency. To the extent that tort costs borne by businesses are the equivalent of a tax, we also estimate the potential impact on employment of "tort tax" relief that would result from improvements to the legal environment in individual states. In this way, we identify opportunities to promote economic activity by improving a given state's legal environment to the level already achieved by the benchmark states.

We measure the relative costs of the legal environment in each state by determining how much of the variation in tort costs across states is explained by corresponding variation in a "Legal Environment Benchmark." This Legal Environment Benchmark is composed of a "Tort Activity Index," and a measure of the perceived fairness and reasonableness of the tort system. The Tort Activity Index consists of three

## POTENTIAL 2009 TORT COST SAVINGS AND EFFECT ON BUSINESS ACTIVITY FROM IMPROVEMENTS IN THE LEGAL ENVIRONMENT IN SELECTED STATES

| | | Potential Effect of Legal Environment on Tort Costs | | | Potential Effect on Businesses of Changing Legal Environment | |
|---|---|---|---|---|---|---|
| (1) State | (2) Estimated Tort Costs (millions) | (3) Percent Impact | (4) Dollar Impact (millions) (2)x(3) | (5) Employment (from BLS) (thousands) | (6) Potential Increase in Business Activity | (7) Potential Increase in Employment[1] (5)x(6) |
| California | $32,043 | 16.4% | $5,267 | 16,142 | 0.65 - 1.76% | 104,868 - 283,936 |
| Delaware | $1,027 | 7.1% | $73 | 400 | 0.28 - 0.76% | 1,122 - 3,038 |
| Florida | $15,340 | 18.5% | $2,833 | 8,209 | 0.73 - 1.98% | 59,934 - 162,273 |
| Illinois | $10,446 | 23.3% | $2,435 | 5,928 | 0.92 - 2.50% | 54,626 - 147,903 |
| New Jersey | $9,112 | 21.5% | $1,960 | 4,116 | 0.85 - 2.30% | 35,001 - 94,768 |
| New York | $20,339 | 21.2% | $4,320 | 8,864 | 0.84 - 2.27% | 74,425 - 201,511 |
| Ohio | $8,732 | 12.3% | $1,070 | 5,335 | 0.48 - 1.31% | 25,836 - 69,952 |
| Pennsylvania | $11,991 | 14.3% | $1,719 | 5,867 | 0.57 - 1.53% | 33,255 - 90,041 |

objective measures of tort activity, specifically: the concentration of lawyers, incidence of top verdicts and the volume of tort filings.

The perception of the legal environment is measured using a survey. We rely on the results of the State Liability System Ranking Study conducted for ILR by Harris Interactive Inc. ("Harris") on a representative sample of approximately 1,500 in-house general counsel, senior litigators or attorneys, and other senior executives. Participants grade how fair and reasonable different key elements of the liability system are for the states in which they have experience. Although the rankings are subjective, the econometric analysis provides an objective test of whether or not they help explain the variation in tort costs.

Our study validates the Harris survey results by showing that the rankings are correlated with costs, after removing the effects of economic and demographic factors. The Harris rankings do not measure the fairness and reasonableness of the legal environment with objective certainty, which means that the cost effect that we attribute to this perception measure is likely understated. The Tort Activity Index was also found to be a statistically significant factor in explaining tort cost variations across states.

The costs of the tort system are reflected in the amounts paid in settlements and awards along with the administrative and legal costs of resolving claims. Insurance companies are mandated to report state level data on insured losses and administrative costs. This data provides a detailed source with which to measure variations from state to state.

Of course, not all the variations from state to state are due to features of the legal environment. General economic conditions, such as competition in the insurance market and demographics like the age and employment of the population also affect tort costs. After removing the effects of these economic and demographic factors we determine the amount by which costs consistently change in line with changes in the Legal Environment Benchmark across all states.

It is possible that the states with the best business climate are also less litigious. But we control for this possible alternative explanation for lower liability costs by

including a measure of labor regulation in our analysis to separate out any business climate effect. We find that states perceived to have the most fair and reasonable legal systems, low concentrations of lawyers, few of the largest verdicts across the nation and lower volumes of tort suits tend to have lower tort costs.

The table on the previous page shows how a sample of states measure up in terms of the relative costs of their legal environments in 2009. The estimated costs of the tort system in each state range from $1 billion for Delaware to $32 billion for California. The corresponding total tort system cost for the U.S. in 2009 of $248 billion matches the Towers Watson estimate (although Towers Watson has recently updated this estimate to $252 billion in its U.S. Tort Cost Trends, 2011 Update.)

The effect of the legal environment in each state on the cost of its tort system is also reported. Illinois and New York have the most costly legal environments. In these states we attribute 23 and 21 percent of tort costs, respectively, to characteristics of the legal environment, i.e. perception and measures of tort activity. The state with the least costly legal environment is Delaware. These states could potentially save billions in annual costs by improving their legal environments to match the perception and tort activity levels of the least costly states.

This analysis is based on insurance data for 2009, the most recent year available. However, the analysis could be revised each year to track performance over time. The effects of improvements in the legal environment are expected to take some time to be realized in actual tort costs because new law, procedures and practices may not apply to existing cases. Consequently the frequency of top personal injury verdicts in each state is a lagging performance indicator. Changes in the perception of the legal environment may also take some time to reflect the practitioners own experience of the effects of improvements. Tort filings should be more responsive to changes, making it possible to assess changes as soon as data is reported by the National Center for State Courts.

The scope for improvements in the legal environment in each state can be quantified as the dollar savings from matching the perception and levels of tort activity of the state with the least costly legal environment. The scope would be even larger if greater improvements were achieved.

The potential economic impact of such cost savings goes beyond these direct cost savings of the litigants (and their insurers). Improvements in the legal environment that make litigation risk less costly have the potential to influence business location and expansion decisions and thereby stimulate business activity. Tort costs can be thought of as imposing a tax on businesses and individuals. The effect of changes in this "tort tax" on business activity can be modeled by drawing on prior published studies on the responsiveness of business activity to taxes.

Assuming that a dollar in tort cost reductions would have the same effect as a dollar in tax savings measured in prior studies, a range of potential effects on business activity can be estimated. An individual state with the costliest legal environment that was successful at eliminating this tort cost disadvantage could increase employment by as much as 1.0 to 2.8 percent. The estimated effect of the legal environment on business activity for selected states is reported in the table.

*"The estimated effect of the legal environment on business activity for selected states is reported in the table above. In a large state such as New York or California,* ***eliminating their tort cost disadvantage could add hundreds of thousands of jobs."***

In a large state such as New York or California, eliminating their tort cost disadvantage could add hundreds of thousands of jobs.

The benefits of tort reform are notoriously difficult to estimate. Our study does not measure the effect of specific reforms, but it does provide a measure of the scope for improvements in each state. It also provides a metric for benchmarking and tracking improvements for the future.

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[1]Estimates are for individual states based on the assumption that the legal environments of the other states remain unchanged. These values cannot be added to produce reliable estimates for multiple states.

# Methods of State Judicial Selection: Resources for Legislators

This month the Federalist Society will launch a new website dedicated to providing information about state supreme courts and the way judges are selected. ALEC member legislators with an interest in judicial selection methods should be aware of this resource. To visit the site and access an interactive map of the states go to www.statecourtsguide.com.

Also of help to legislators considering the pros and cons of judicial selection methods, the Federalist Society recently published a survey* of empirical evidence relating to judicial elections. The paper, by Professor Christopher Bonneau from the University of Pittsburgh, examines a number of arguments against judicial elections in the light of empirical evidence relating to those arguments. Below is a summary of his enlightening findings:

### ARGUMENT 1: CAMPAIGN SPENDING IS OUT OF CONTROL AND THE CANDIDATE WHO SPENDS THE MOST MONEY WINS.

Professor Bonneau's response: "In fact, campaign spending is one of the best mobilization agents in state Supreme Court elections. Rather than being alienated by costly campaigns, citizens embrace highly spirited expensive races by voting in much greater proportions than in more mundane contests."[1] Campaign spending allows candidates to provide voters with information. This information is then used by voters to help them make a decision in the race.[2] In this way, campaign spending benefits voters by allowing candidates to run a vigorous campaign and make their case to the voter.

Additionally, at the intermediate appellate court level, Streb and Frederick[3] find that the spending difference between candidates is not a significant predictor of vote total (although it is significant for incumbents who were initially appointed and thus are making their first run for the bench). At the trial court level, systematic research has yet to be conducted.

### ARGUMENT 2: JUSTICE IS FOR SALE.

Professor Bonneau's response: "The literature on this is mixed. Some scholars have found a correlation between campaign contributions and judicial decisions[4] while others have not, at least under some conditions.[5] We simply do not know. Establishing causality (and not simply a correlation) can be methodologically tricky."

The methodological problem is summarized succinctly by Cann[6]: "They argue that a correlation between campaign contributions and judicial decisions exists because contributions from attorneys on the liberal (or conservative) side of a case lead judges to reciprocate by voting in a liberal (or conservative) way. But it may be that attorneys who generally find themselves on the liberal (or conservative) side of a case contribute to candidates who are already likely to rule in a liberal (or conservative) direction. This contribution strategy increases the chances of their preferred candidate winning. If their candidate is elected, they are more likely to win cases before them, not because the judge's vote was influenced by the campaign contribution, but because it was the judge's propensity to vote in a particular way that led to the contribution in the first place."

Hence, the question of whether justice is "for sale" is very much an open question.

### ARGUMENT 3: JUDICIAL ELECTIONS LEAD TO A LOSS OF LEGITIMACY.

Professor Bonneau's Response: Gibsonet. al.[7] examined whether the positives from judicial elections outweigh the negatives.

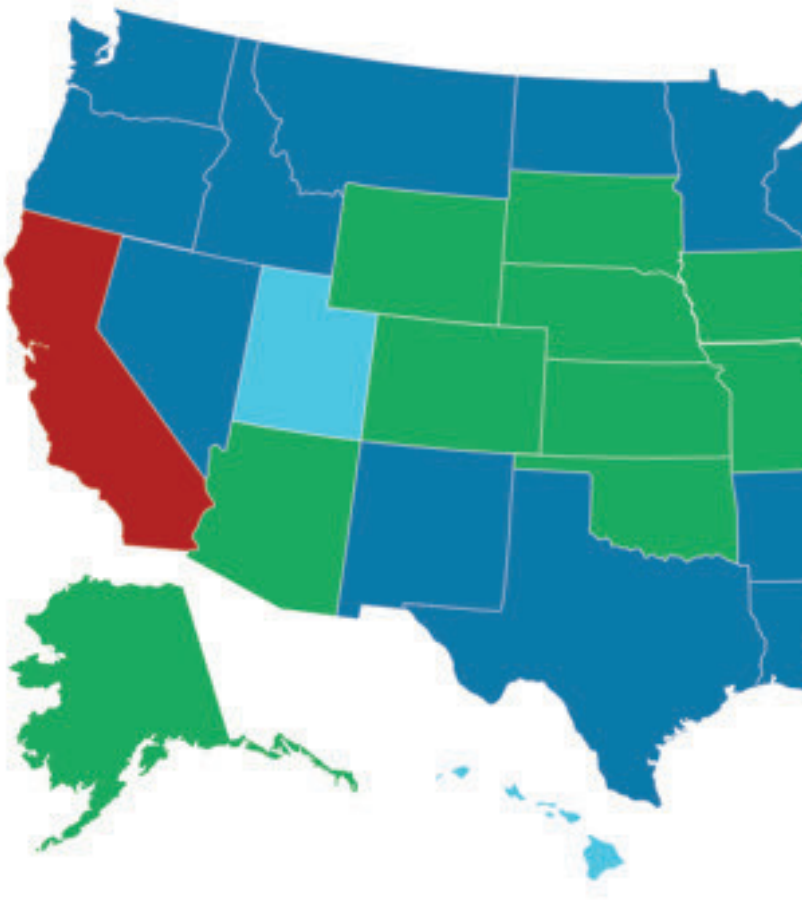
Using a survey experiment conducted in Pennsylvania in 2007, the authors found that, "Elections by themselves seem to generate more support for the judiciary; these data do suggest that courts do in fact profit to some degree from their periodic encounters with voters. At the same time, however, the positive effect of elections is dampened by the campaign ads that associate courts with ordinary voters. The effect is not great, and not great enough to neutralize entirely the positive consequences of exposure to the judiciary."[8] That is, the net effects of elections are positive. Elections serve to enhance the legitimacy of the office.

### ARGUMENT 4: JUDGES CHANGE THEIR DECISIONS ON CASES WHEN THEY NEED TO FACE THE ELECTORATE.

Professor Bonneau's Response: Brace and Boyea[9] demonstrate that "elections and strong public opinion exert a notable and significant direct influence on judge decision making in these cases, but these effects do not outweigh the impact of case characteristics and judge ideology." Thus, while elections are important, they are not as important as the facts of the case and the ideology of the judge. Additionally, while one could conclude that judges are not following the law because they are afraid of losing their jobs, one could also argue that the evidence shows the electorate is forcing the judges to do their jobs (instead of following their own personal predilections) or risk losing an election.

### ARGUMENT 5: VOTERS DO NOT PARTICIPATE IN THESE ELECTIONS.

Professor Bonneau's Response: Hall[10] and Bonneau and Hall[11] find that, contrary to claims otherwise, state Supreme Court elections are not universally characterized by a lack of participation by the public. From 1990-2004, average roll-off[12] was 22.9% for all elections. So, roughly 75% of the people who turned out to vote actually cast a ballot for state Supreme Court judge. Further, when one looks at contested races (races where there was more than one



**ELECTIONS**
Judges are directly elected by the voters of the state.

**Partisan**

Alabama
Illinois
Louisiana
New Mexico
Pennsylvania
Texas
West Virginia

**Nonpartisan**

Arkansas
Georgia
Idaho
Kentucky
Michigan
Minnesota
Mississippi
Montana
Nevada
North Carolina
North Dakota
Ohio
Oregon
Washington
Wisconsin

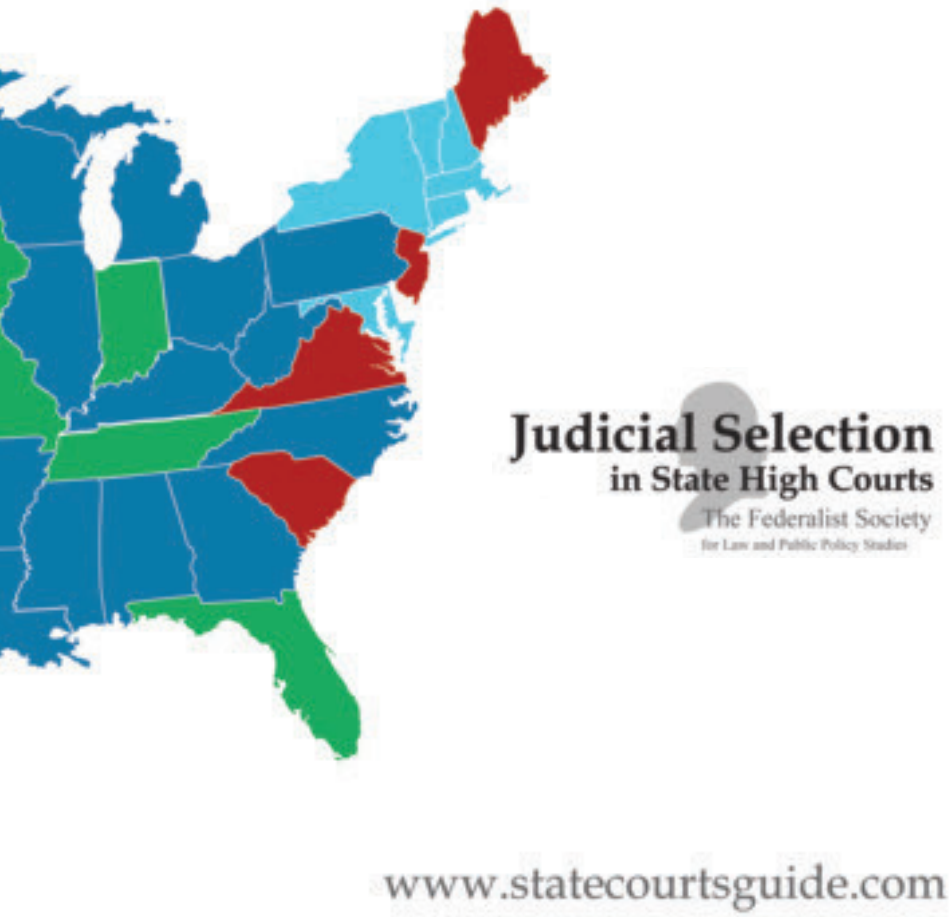
**DEMOCRATIC APPOINTMENT**
Judges are appointed directly by a democratic body, or appointed by the governor with the advice and consent of a democratic body. (Note: Democratic body = popularly-elected officials or judges nominated and confirmed by popularly-elected officials.

**Gubernational**

California
Maine
New Jersey

**Legislative**

South Carolina
Virginia




**MISSOURI PLAN**
Judges are appointed by the governor after nomination by a commission without confirmation by a democratic body.

**Role for Bar**

Alaska
Arizona
Florida
Indiana
Iowa
Kansas
Missouri
Nebraska
Oklahoma
South Dakota
Wyoming

**No Role for Bar**

Colorado
Tennessee

**HYBRID**
Judges are appointed by the governor after nomination by a commission and confirmed by a democratic body.

Connecticut
Delaware
Hawaii
Maryland
Massachusetts
New Hampshire
New York
Rhode Island
Utah
Vermont

candidate seeking the position), the roll-off rate decreases to 16.1%. Finally, if one looks at contested partisan elections (where voters are provided the partisan affiliation of the candidates on the ballot), roll-off is even lower: 11.1%.[13] More importantly, "higher amounts of campaign spending produce significantly lower levels of ballot roll-off."[14]

### ARGUMENT 6: VOTERS DON'T KNOW WHO THEY ARE VOTING FOR.

Professor Bonneau's Response: Bonneau and Hall[15] find that a challenger who has prior judicial experience performs about 4.7% better against an incumbent than a challenger without such experience. This is substantively important because "given that the average incumbent's vote is only 56.8 percent during the time frame of our study, the challenger's relative experience or inexperience could well mean the difference between an incumbent's re-election and defeat in many of these contests".[16] Thus, it appears that voters are able to recognize incumbents who are ideological outliers (at least in partisan elections) and distinguish between higher qualified alternatives to incumbents and lower qualified alternatives. In the aggregate, then, voters appear to have enough information to make an informed decision in the election.

### ARGUMENT 7: INCUMBENTS ARE RARELY CHALLENGED AND NEVER LOSE AND THUS ARE NOT ABLE TO BE HELD ACCOUNTABLE.

Professor Bonneau's Response: The re-election rate of incumbents shows that these judges have something real to fear if they are challenged. From 1990-2004, Bonneau and Hall[17] show that the re-election rate for members of the U.S. House was 94.9 percent; for the Senate, 90 percent; and for governors, 81.1 percent. State Supreme Court justices were re-elected 91.3 percent of the time, about the same as for members of the Senate. Moreover, when you look just at partisan elections (which elections for the House, Senate, and Governor all are), state Supreme Court incumbents won reelection only 68.8 percent of the

time. That is, in the races most comparable to races for other statewide elected offices, state Supreme Court incumbents have the most to fear in terms of losing their jobs.

### ARGUMENT 8: ELECTED JUDGES ARE NOT AS QUALIFIED AND ELECTIONS LEAD TO LESS DIVERSITY ON THE BENCH.

Professor Bonneau's Response: Stephen Choi, G. MituGulati, and Eric Posner[18] set out to test whether elected judges perform better or worse, once on the bench, than appointed judges. They measured the performance of judges on three dimensions: productivity, citations, and independence. Their results fly in the face of conventional wisdom: "We find that elected judges are more productive. And although appointed judges write opinions that are cited more often, the difference is small and outweighed by the productivity difference. In other words, in a given time period, the product of the number of opinions authored and citations-per-opinion is higher for elected judges than for appointed judges."[19] Additionally, Frederick and Streb[20] find that, "If any verdict can be reached on the role of sex in the outcomes of judicial elections, then it is that women might receive a modest boost at the polls." In sum, the bulk of the evidence suggests that there is no relationship between diversity and the method of selection.[21]

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[1]Chris W. Bonneau& Melinda G. Hall, In Defense of Judicial Elections (2009) at 131.

[2]Lawrence Baum, Judicial Elections and Judicial Independence: The Voter's Perspective, 64 Ohio St. L.J. 13 (2003).

[3]Matthew J. Streb& Brian Frederick, Conditions for Competition in Low-Information Judicial Elections: The Case of Intermediate Appellate Court Elections, 62 Pol. Res. Q. 523 (2009).

[4]Damon Cann, Justice for Sale? Campaign Contributions and Judicial Decisionmaking, 7 St. Pol. Pol'y. Q. 281 (2007); Madhavi McCall, The Politics of Judicial Elections: The Influence of Campaign Contributions on the Voting Patterns of Texas Supreme Court Justices, 1994-1997, 31 Pol. &Pol'y 314 (2003); Joanna M. Shepherd, Money, Politics and Impartial Justic, 58 Duke L.J. 623 (2009).

[5]Damon M. Cann, Campaign Contributions and Judicial Behavior, 23 Am. Rev. Pol. 261 (2002); Damon M. Cann et al., New Directions in Judicial Politics, (Kevin T. McGuire ed., 2012).

[6]Cann, Justice for Sale?,supra, at 284.

[7]James Gibson et al., The Effects of Judicial Campaign Activity on the Legitimacy of Courts: A Survey-based Experiment, 64 Pol. Res. Q. 545 (2011).

[8]Gibson et al., supra, at 553.

[9]Paul Brace & Brent D. Boyea, State Public Opinion, the Death Penalty, and the Practice of Electing Judges, 52 Am. J. Pol. Sc. 360, 370 (2008).

[10]Hall, Voting, supra.

[11]Bonneau& Hall, supra.

[12]"Roll-off" is the percentage of voters who go to the polls but do not vote for the judicial races.

[13]For more information, see Tables 2.1 and 2.2 in Bonneau and Hall, supra.

[14]Bonneau& Hall, supra, at 44.

[15]Bonneau& Hall, supra.

[16]Bonneau& Hall, supra, at 98.

[17]Bonneau& Hall, supra.

[18]Stephen J. Choi et al., Professionals or Politicans: The Uncertain Empirical Case for an Elected Rather than Appointed Judiciary, 26 J.L. Econ.& Org. 290 (2010).

[19]Id. at 292.

[20]Brian Frederick and Matthew J. Streb, Women Running for Judge: The Impact of Sex on Candidate Success in State Intermediate Appellate Court Elections, 89 Soc. Sci. Q. 937, 950 (2008).

[21]Margaret Williams finds that "nonpartisan elections affect women's representation on trial courts, while merit selection affects representation on appellate courts." Margaret Williams, Women's Representation on State Trial and Appellate Courts, 88 Soc. Sci. Q. 1192, 1200 (2007). However, it is unclear what to make of this finding given the way she codes the method of selection. Williams codes these "based on the method by which a majority of the judges at that level reached the bench." Id. at 1196-97. Since the state is the unit of analysis here, this means that if a state elects trial court judges in partisan elections but appoints appellate court judges, the state is coded as partisan since there are more trial court judges than appellate court judges. See FN5, supra. This makes it difficult to ascribe any influence to method of selection.


# Energy on Trial: Environmentalists Pollute the Legal System

BY BRYAN WEYNAND

From state attorneys general, to municipal leaders, to plaintiff's lawyers, and even down to ordinary activists, there is an emerging trend in the environmental movement that binds together its misguided attempt to force a rapid transition toward renewable energy. Demonstrating their disdain for both fossil fuels and existing legal processes and institutions, each of these parties have used legal claims as an end-justifies-the-means avenue for delaying or inhibiting the use of such fuels; even as improved technology offers a way toward cleaner use, energy independence, and a step toward economic recovery.

The three separate issues of public nuisance litigation over greenhouse gas emissions, frivolous litigation regarding natural gas drilling, and municipal bans on hydraulic fracturing together illustrate this trend, which should serve as a red flag of caution for potential exploitation of our nation's civil justice system for political purposes. As they are undeterred by their vision's lack of economic viability, they will not be discouraged when, even lacking a strong legal argument, they can effectively discourage future use of fossil fuels by imposing barriers and costs through drawn out litigation.

## GREENHOUSE GAS LITIGATION

In the case of public nuisance litigation over greenhouse emissions, the attempt of eight states and New York City to sue the nation's five largest emitters has already been dealt a significant blow. The Supreme Court held in *AEP v. Connecticut* that the plaintiffs' request for injunctive relief was displaced by the *Clean Air Act* and the authority it grants to the federal Environmental Protection Agency.[1] However, as attorneys Richard Faulk and John Gray wrote after the case, many questions remain over the potential for future climate change litigation, and it is therefore premature to declare the threat resolved.[2]

The impetus for the case, filed in 2004, was the public policy goal of capping greenhouse gas emissions. The plaintiffs claimed that these emissions violated the common law of nuisance by contributing to global warming and, interestingly, asked the court to implement a cap rather than award damages.

From the beginning, the plaintiffs had little expectation of success. The Supreme Court had previously held in *Massachusetts v. EPA* that authority to regulate greenhouse gases had been asserted by Congress and delegated to the EPA, concluding that these institutions were handling the issue in the proper venue and that this displaced the right to a public nuisance claim.[3] There was never any reason to suggest that the question could or should be handled in the judiciary, and only a group of activist attorneys general, determined to impose a defeated legislative and regulatory agenda through litigation, could make such a claim.

Yet further questions remain because of the narrowness of the decision. Because the court dispensed with the claim merely on the basis of its displacement by the *Clean Air Act*, it did not resolve broader questions, such as whether claims could be brought under state common law, or whether claims that seek damages rather than injunctive relief may have more success. Despite the strong arguments that practicality renders this issue political and thus not justiciable, the Court held in a 4-4 tie that other than the displacement argument, "no other threshold obstacle bars review" of the claim. In other words, part of the court remains open to considering emission of greenhouse gases as a public nuisance, provided the plaintiffs seek damages rather than displacement of regulatory authority.

These questions may present themselves to the court in the imminent future as the case *Native Village of Kivalina v. ExxonMobil* works its way through appeal. In the meantime, as noted by Faulk and Gray, "AEP's failure to deliver a definitive 'knockout' probably encourages public nuisance advocates to persist in their quest."[4]

Moreover, as civil justice reform advocates know well, litigation for damages can be a concerning but effective regulatory tool by imposing excessive costs that deter future action. That such claims could be accepted raises the possibility of a foreboding invitation for similar litigation against greenhouse gas emitters across the country. While environmentalists would not have achieved their regulatory vision, in this scenario, they would have at least partially succeeded in using their frivolous claims to obstruct the production of electricity from fossil fuels.

> *"Even as the trial bar maintains a target on the industry, environmentalists are likely hopeful that the litigation could deter future expansion of natural gas drilling."*

## NATURAL GAS

It is now well documented that technological advancements have opened up access to a wealth of recoverable domestic natural gas, and for years the environmental community touted natural gas as a cleaner alternative to coal for producing electricity. Yet now that natural gas shows the potential to displace the environmental basis for renewable energy, they are now going on the attack against the industry.

Widespread fear mongering related to hydraulic fracturing and allegations of deceptive practices related to drilling leases offer a range of incentives to invite litigation, and in fact, there is significant evidence that the trial lawyer community already has the industry in its sight as its next lucrative target.

Last year, a national trial bar conference held a seminar titled "Unconventional Gas Drilling & Fracking: Technology, Law & Regulation," which detailed the "ins and outs of this emerging environmental controversy" for litigators hoping to capitalize. More recently, the Oil and Gas Litigation Group of the American Association for Justice (AAJ), the nation's most prominent trial bar lobby, held a similar meeting to educate attorneys on how to sue drillers.

Current lawsuits in Texas, New York and Pennsylvania claim nuisance and negligence and seek damages for loss of drinking water, decrease in property value, emotional harm, and exemplary damages.[5] A recent *New York Times* article on the industry titled

"Learning Too Late of the Perils in Gas Well Leases" makes victims of landowners who rushed into signing profitable leases before regretting the terms later, and it was this topic that drew the primary focus of the AAJ seminar.

In the case of the groundwater contamination cases, there is already reason for skepticism. The plaintiffs in the New York case, *Baker, et al. v. Anschutz Exploration Corporation, et al*, seek $150 million in compensatory damages, punitive damages, and future medical monitoring for cancer due to the supposed release of gas into water wells because of negligent design. Yet the New York Department of Environmental Conservation has published a detailed investigation that rebuts the plaintiffs' claim, concluding that the drilling was not the cause of the well contamination.[6] The public efforts by the firm litigating the case to link the contamination to hydraulic fracturing at large have led to speculation that it represents a stunt to gain the business of future plaintiffs, and a prominent industry attorney called the case a "precursor to future litigation."[7]

As the trial bar maintains a target on the industry, environmentalists are likely hopeful that the litigation could deter future expansion of natural gas drilling. While President Obama's EPA has been unfriendly to the industry in launching duplicative regulatory programs, he does not seek to halt hydraulic fracturing, and state regulatory agencies and legislatures—such as those in Pennsylvania—have legitimized the practice. Once again, activists will continue to resort to alternative means to impose their vision of limiting fossil fuel use—and frivolous litigation is a likely component of their strategy.

## MUNICIPAL BANS ON HYDRAULIC FRACTURING

A separate but equally frivolous attempt to obstruct hydraulic fracturing through litigation involves municipal governments making spurious constitutional claims rather than plaintiffs making spurious tortious claims.

Local governments in Pennsylvania, West Virginia, New York, Ohio, and Maryland—including those in Pittsburgh, Buffalo and Morgantown—have passed bans on the practice that assert a right to local self-governance over state regulatory preemption.

There is an obvious irony in the environmental movement's selection of local property rights as a defense. In reality, it illustrates not a consistent defense of decentralized governance, but a concession that, at least regarding a total ban, they have lost the battle on hydraulic fracturing at the federal and state level.

Even the preeminent states' rights advocate James Madison was wary of the ability of decentralized government institutions to violate the liberties of their citizens, and he saw the protection of the people against their local and state governments as one the core functions of the tightly limited federal government created by the Constitution. Municipal bans on hydraulic fracturing represent such a case: not an exercise of local governance, but an affront to the liberty of property owners who wish to profit from drilling on their land, one that is legally preempted by the state regulatory scheme.

Though advocates have presented their argument in constitutional terms, there is little legal case to be made for their alleged authority. The Morgantown ban has already been struck down in court, and the bans in other places are merely waiting for a challenger before likely seeing a similar result.

Yet as one legal commentator wrote on the Pittsburgh ban, "Any challenge will result in a show trial, and even where Pittsburgh loses (and it will lose), the forces behind the ordinance win (and the taxpayers footing the legal bills lose)."[8] Taxpayers lose not only the expense of the legal bills, but the revenues from drilling and most significantly, the resulting economic activity and jobs. Local leaders in some towns have justified the unconstitutional bans by touting the delays and costs imposed on drillers, which accomplish virtually the same goal as a ban. There could be no clearer expression of a willingness to flout the legal system in pursuit of a frivolous, end-justifies-the-means environmental agenda.

Each of these cases pose different challenges that will need to be met by different solutions, but collectively they present an alarming trend to the legal and business community. The radical approaches of the environmental movement have been well chronicled. Yet as it continues to lose battles in state legislatures and in the federal Congress, it is their exploitation of the civil justice system in pursuit of political goals that is becoming a trademark of the movement.

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[1]http://www.supremecourt.gov/opinions/10pdf/10-174.pdf

[2]http://www.gardere.com/Binaries/Press%20and%20Publications/20110815AEParticleFAULKGRAYARTICLE.pdf

[3]http://www.supremecourt.gov/opinions/06pdf/05-1120.pdf. It is important to note that ALEC believes this decision to be wrongly decided and does not share the notion that the Clean Air Act authorizes EPA regulation of greenhouse gases as a pollutant. However, that the question of whether regulation of air quality requires limiting greenhouse gases rests with Congress and the EPA is clear.

[4]http://www.gardere.com/Binaries/Press%20and%20Publications/20110815AEParticleFAULKGRAYARTICLE.pdf

[5]http://www.frackinginsider.com/litigation/the-plaintiffs-bar-zeros-in-on-fracking/

[6]http://www.scribd.com/doc/61955915/NYS-DEC-November-2010-Fact-Sheet-on-Big-Flats

[7]http://www.frackinginsider.com/litigation/hydraulic-fracturing-fracking-during-natural/

[8]http://jurist.org/dateline/2011/07/joseph-schaeffer-hydraulic-fracturing.php

# Medicaid Agencies Can Successfully Address Increasing Costs with Radiology Benefits Management Programs

BY NORMAN A. SCARBOROUGH, M.D.

While the current recession has impacted Americans, businesses, and government programs throughout the nation, few are experiencing a financial strain more than Medicaid agencies. According to the Kaiser Commission on Medicaid and the Uninsured, "since the start of the recession, Medicaid enrollment has grown by 8.8 million," pushing overall enrollment to 51.5 million.[1] Maintaining this level of enrollment has forced states to seek ways to save money without negatively impacting beneficiaries.

One way some states are controlling costs, while continuing to support this unprecedented growth, is by implementing radiology benefits management (RBM) programs. RBM programs reduce the overuse of advanced diagnostic imaging procedures. The procedures addressed by RBM programs typically include computerized tomography (CT) scans, magnetic resonance imaging (MRI), and positron emission tomography (PET).

RBM programs have been adopted by commercial health insurance companies for decades and are successfully used by some of the nation's largest insurers, including Aetna, CIGNA, UnitedHealthcare, and Humana. According to an article published in the *Radiology Business Journal* in July 2009, it is estimated that RBM programs cover approximately 100 to 130 million health insurance members in the United States and have saved health insurance companies hundreds of millions of dollars.[2]

Despite the success of RBM programs in the commercial health insurance sector, states have been slow to adopt them—but that has changed due to the pressures placed on Medicaid agencies to become more financially efficient. Medicaid agencies that have adopted RBM programs have significantly decreased costs associated with beneficiary imaging services, while increasing the quality of patient care and maintaining high levels of physician and beneficiary satisfaction.

When an RBM program is implemented by a health plan, providers submit authorization requests to the RBM organization prior to patients receiving advanced imaging procedures. These requests are reviewed for appropriateness. Ideally, these decisions are determined using evidence-based guidelines that are created through the integration of well-known and widely accepted medical society standards and current medical literature, as well as input from recognized clinical subject matter experts. High quality RBM programs also support the prior authorization process with clinical staff experienced in the appropriate use of diagnostic radiology, offering providers additional resources to assist with their advanced imaging requests.

RBM programs have become a necessity for insurers seeking to decrease costs due to the increased growth in advanced imaging utilization. America's Health Insurance Plans (AHIP) has stated that diagnostic advanced imaging costs are reported to be the fastest growing component of medical technology, with spending approaching $100 billion annually. Several factors contribute to this increase in imaging, including:

- Use of services that were previously unavailable or difficult to access.
- Adoption of emerging technologies without education on their appropriate use and how they contribute to clinical situations.
- Quality issues that result in the duplication of procedures due to the ineffectiveness of initial scans.
- Rise in self-referrals, with providers ordering advanced imaging procedures for their patients and either performing the procedure themselves or having the procedure completed at a facility from which they receive a financial incentive. According to a 2002 article in the American Journal of Roentgenology, self-referring physicians performing their own imaging "are at least 1.7–7.7 times as likely to order imaging as non–self-referring physicians in the same specialty who see patients with the same problems." Advanced imaging procedures were ordered as much as 54 percent more often by physicians with ownership interests in outside facilities than by non-self-referring physicians.[3]
- Defensive medicine practices, with physicians ordering procedures to protect them against litigation in the event of an unfavorable patient outcome. According to one report, the practice of defensive medicine costs the United States healthcare system from $60 billion to $108 billion annually.[4]

RBM programs offer more than just financial benefits to Medicaid programs. Many patients and healthcare providers are unaware of the significant health risks which may be associated with some advanced imaging procedures. *HealthLeaders Media* stated in 2009 that "the National Cancer Institute estimates nearly 30,000 excess cancers occurred from the 72 million CT scans in the U.S. just in 2007. About half of those cancers may be lethal."[5] By evaluating

a provider's advanced imaging request and confirming its appropriateness, RBMs help eliminate unnecessary radiation exposure, which reduces patient safety risks and future healthcare issues, as well as the costs for treatment.

RBM programs have been proven to reduce the financial burden of advanced imaging overutilization within America's healthcare system. RBM programs are so successful that in June 2011, the Medicare Payment Advisory Commission (MedPAC) recommended that the U.S. Congress implement a prior authorization program in Medicare to address practitioners who order a substantially larger number of advanced imaging services than their peers.[6] In addition to assisting with the financial burdens experienced by Medicaid agencies, states have also applied prior authorization services to state employee health plans, resulting in significant savings.

States considering an RBM program should thoroughly review several factors before choosing an appropriate organization to provide these services. Medicaid programs operate differently from commercial insurers, so selecting an RBM organization with extensive experience with both fee-for-service and managed Medicaid programs would be ideal.

Various contracting models are also available. One example is an administration-only model where the state pays fees to the RBM organization for operating the program, which leaves the state vulnerable to possible fluctuations in costs. Another example is a capitation model where the RBM organization manages the advanced imaging program for the state and assumes any financial risk due to cost fluctuations. This second model is more advantageous because the RBM organization provides the state with guaranteed savings. It also allows the state to know how much they will spend on advanced imaging during the contracted period, as the RBM program assumes the financial risk if the program's requirements exceed the established budget.

Medicaid programs will continue to experience increasing populations as eligibility expansion begins in 2014, based on the new rules established by the *Patient Protection and Affordable Care Act.* According to the Centers for Medicare and Medicaid Services, Medicaid programs are projected to add 11.6 million people, a 21 percent increase, to existing enrollments in 2014, and almost 20 million people, a 34 percent increase, by 2019.[7] To address these enrollment increases, states must seek ways to reduce costs, while continuing to offer services that are vital to their populations. RBM programs are a viable and proven option. States should take note of the successes experienced by other insurers that have implemented RBM services and consider the potential benefits for their Medicaid programs and beneficiaries.

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[2]Wiley, George, "RBMs: The Debate Heats Up," Radiology Business Journal (July 01, 2009): http://www.imagingbiz.com/articles/view/rbms-the-debate-heats-up/.

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# Complications with the EPA's Utility MATS and Cross State Air Pollution Rule

BY JON MCKINNEY

In the past few years, the U.S. Environmental Protection Agency (EPA) has promulgated a number of regulations that directly affect the generation of electricity. Two of these rules, the Cross State Air Pollution Rule and the Utility Mercury and Toxic Substances (MATS) rule, will significantly impact cost and reliability. The Cross-State Air Pollution Rule aims to reduce power plant emissions that cross state lines. This rule was recently stayed by the court, yet utilities are still expecting to have to comply at some point in the future despite evidence that the reductions in emissions have already been met. The MATS rule, also known as the Utility MACT rule, aims to further regulate hazardous air pollutants, including mercury and acid gases, for coal and oil plants. This rule has an unreasonably and unnecessarily short timeline for compliance, and the standards are so stringent that no new coal plants are likely to be built.

## MATS COMPLIANCE DEADLINE IS NOT A SATISFACTORY OPTION

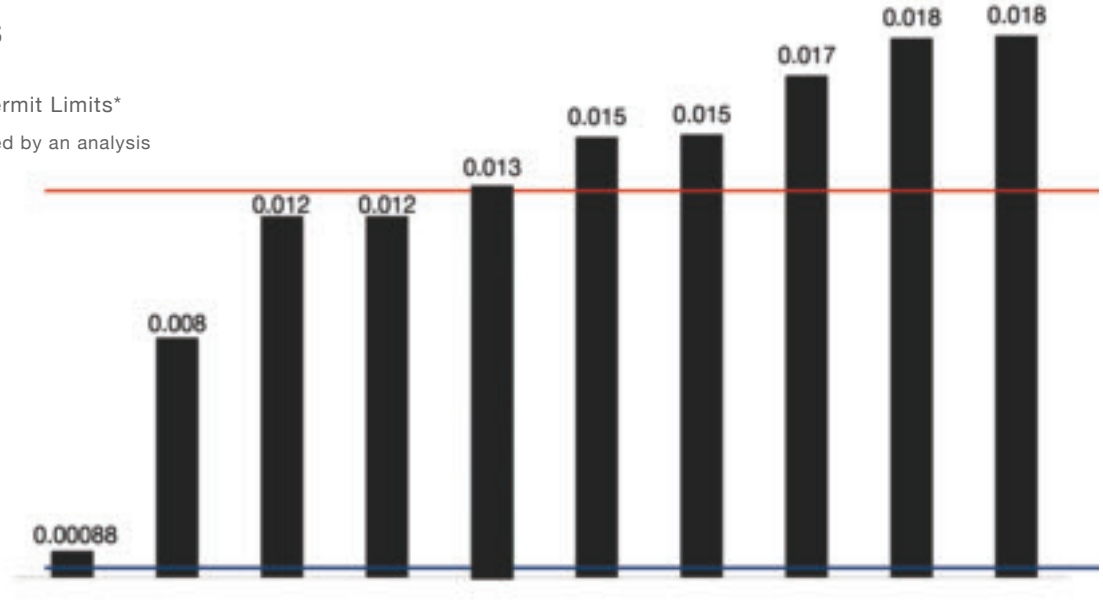
EPA published the finalized MATs rule in February 2012. The compliance period will start on April 16, 2012, and affected power plants will have to comply with the standards by April 16, 2015. The EPA has allowed for an extra year for compliance as the original three year compliance timeline was thought to be untenable. In specific cases affecting reliability, the rule allows for a fifth year for compliance, yet it is not a satisfactory flexibility option—it would effectively require states and generators to violate the *Clean Air Act* first. The final rule includes a fifth year for units that are critical to reliability which can be given through a Consent decree—but only if the plant violates the *Clean Air Act* first by exceeding applicable emissions limits. No state or plant owner wants to base its plans on being in non-compliance.

As an example of issues that this can cause, MIRANT, an Atlanta-based energy company that produces and sells electricity, was the target of civil environmental suits when it was directed to run two plants to maintain reliability.

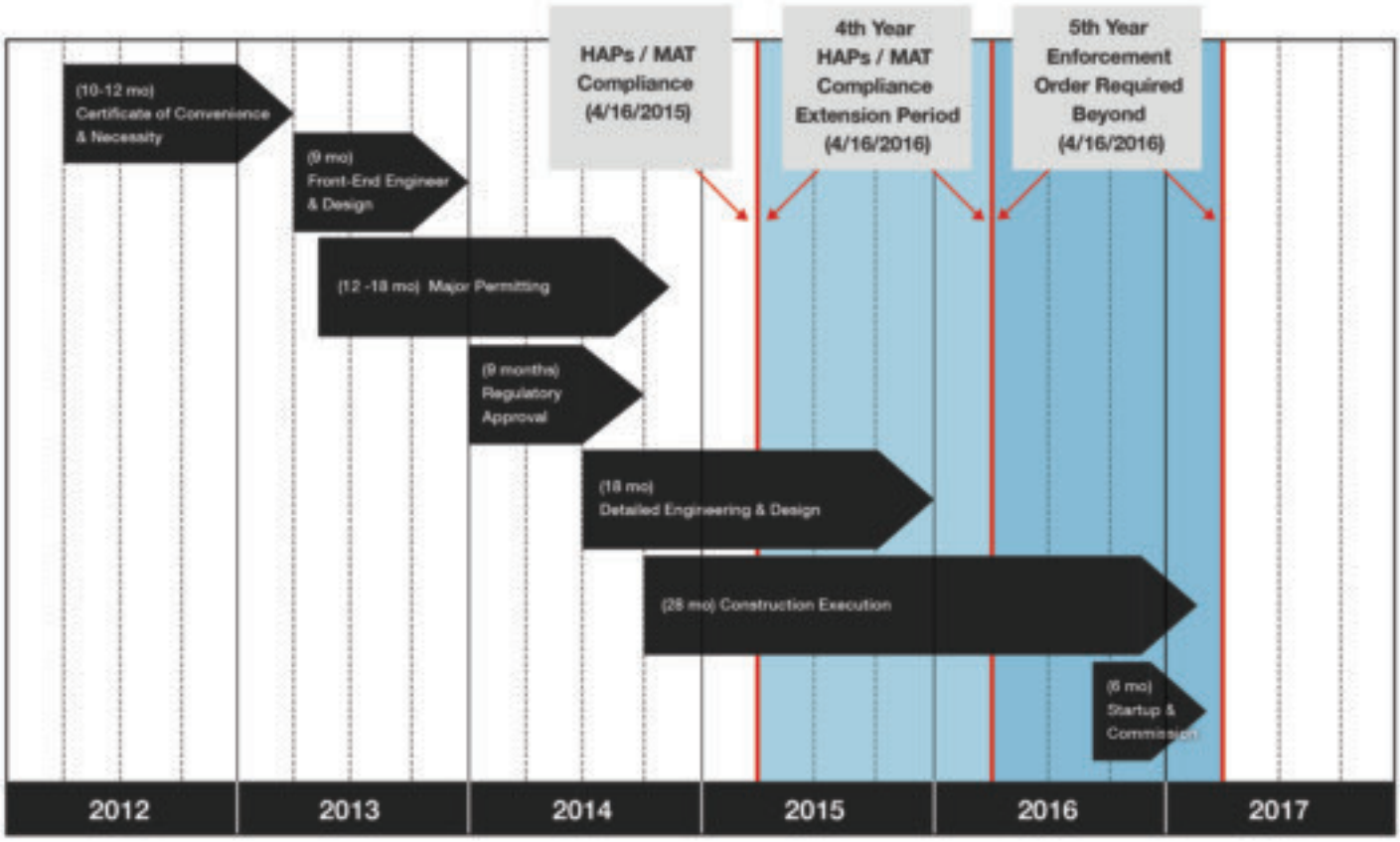
## NEW SOURCE MERCURY MATS

Mercury MATS vs. Current Air Permit Limits*
(*most stringent permit limits identified by an analysis of new coal units built since 2001)

Note: Historically, mercury limits have been based on annual averages. The Final MATS applies a more stringent 30-day average.
Source: Derived from AEP MATS Comments to U.S. EPA (2011).



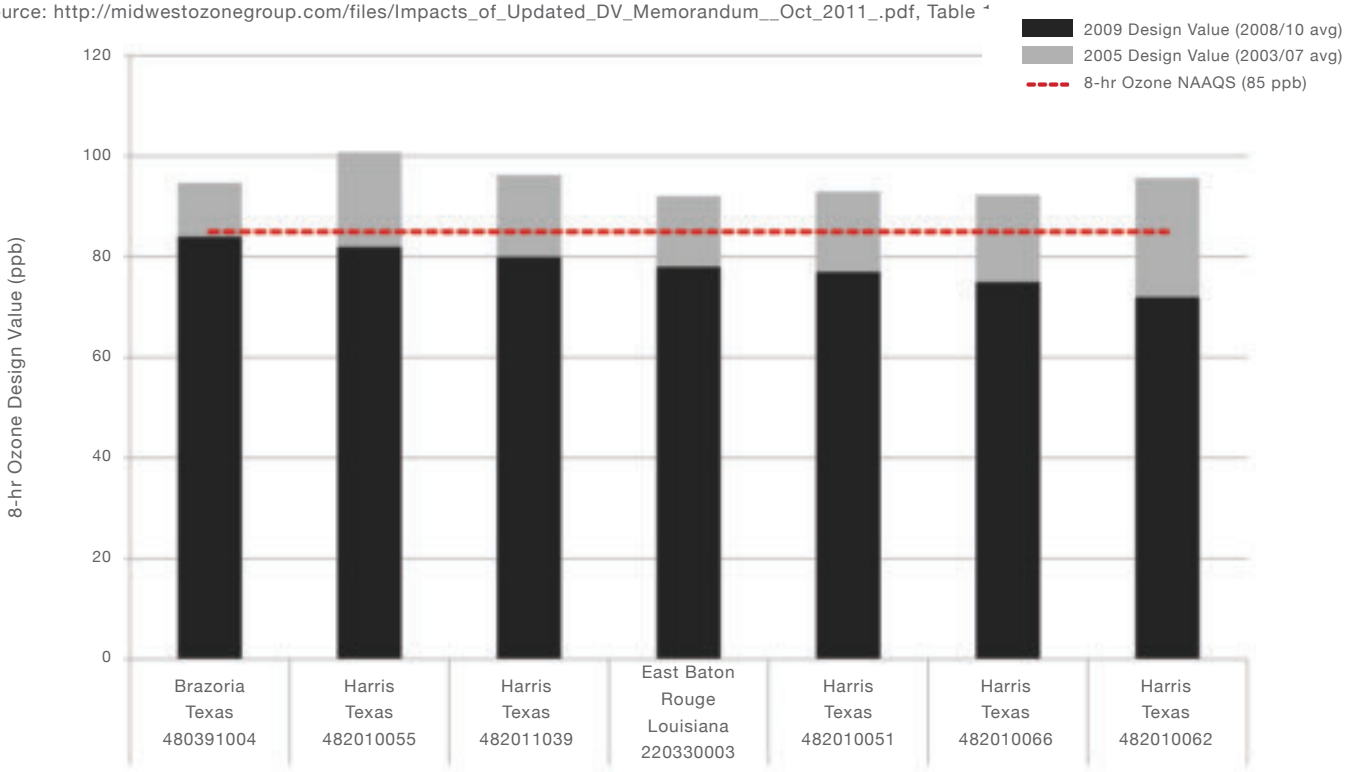

## THE KEY PROBLEM:
## INADEQUATE FGD RETROFIT TIME EVEN WITH 4TH YEAR; 5THYEAR LIMITED TO "RELIABILITY CRITICAL" UNITS




The 4th Year Extension Period provides some relief to the construction schedule. However, units with complianceprojects that extend beyond the 4th Year Extension Period that have no transmission reliability consequences will be forced to come off line.

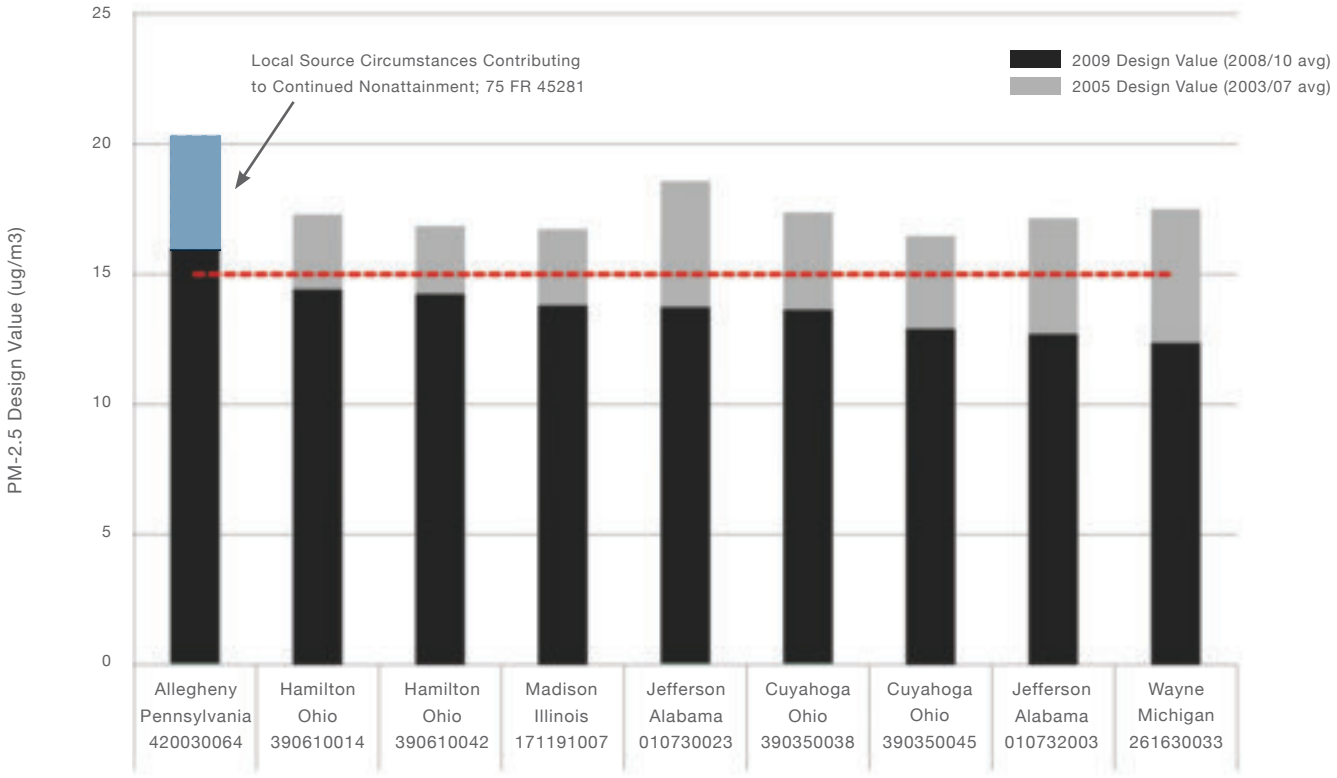
## COMPARISON OF AVERAGE 8-HOUR OZONE AIR QUALITY AT PROJECTED CSAPR NONATTAINMENT SITES 2005 VS. 2009

Source: http://midwestozonegroup.com/files/Impacts_of_Updated_DV_Memorandum__Oct_2011_.pdf, Table 1




## COMPARISON OF AVERAGE ANNUAL PM2.5 AIR QUALITYAT PROJECTED CSAPR NONATTAINMENT SITES 2005 VS. 2009

Source: http://midwestozonegroup.com/files/Impacts_of_Updated_DV_Memorandum__Oct_2011_.pdf,



Commissioners are well aware that regulatory approval processes are subject to delays due to intervenor and other interests that we must take into account. For example, the Sierra Club claims to have blocked 150 proposed coal plants by intervening in regulatory proceedings and is now aiming to shut down 500 plants that are still operating, according to its web site. The club has already intervened in proceedings for retrofits. These concerns about regulatory delays apply equally to the fourth year time extension that the EPA has provided to states.

Five to six years to complete retrofit activities is the rule, not the exception, for projects regulators have previously approved. Three years are usually needed for pre-construction engineering activities and regulatory approvals before construction actually begins.

These concerns about delays apply equally to the fourth year time extension that the EPA has provided to states.

Federal legislative action, such as the Manchin-Coats Fair Compliance Act is needed to provide certainty and harmonize EPA deadlines with real world pre-construction and construction timelines.

## NO NEW COAL PLANTS

Although the EPA has flexibility in setting standards for new coal-fired plants that reflect real world operating conditions and technology capabilities, the standards of the MATS rule are so stringent that even recently permitted plants employing best available technology cannot meet them and no new coal plants are likely to be built. These new source standards are supposed to reflect the capabilities of emission control technologies in use now by the best performing coal units in the United States but do not.

For example, the mercury standard for new sources is 0.0002 lb/GWh, less than 2 percent of the average for the 10 best plants recently permitted after Best Available Control Technology reviews. To meet the new source limits, plants will have to operate well beyond manufacturer performance guarantees and achieve emission limits that are so low that detection limits are below available monitoring equipment capability.

## IS THE CROSS STATE AIR POLLUTION RULE (CSAPR) NEEDED?

As explained in a December 22, 2011, *Fort Wayne Journal Gazette* op-ed by five state environmental regulatory officials, when using the latest data from EPA monitors, the air quality objectives of CSAPR already have been achieved and consumers will be paying for a regulation that is not needed.

In this case, the EPA is not giving credit for air quality improvements resulting from investments totaling billions of dollars that Commissions approved. West Virginia alone has spent $4 billion that monitors now show have improved levels to below the target level for CSAPR.

## GRID RELIABILITY

The EPA projects approximately 5GW of plant retirements from its regulations while the industry has announced it intends to retire more than10 times that amount.

PJM and the Southwest Power Pool, two large regional transmission organizations which deal with reliability of electricity, have requested that companies provide their compliance plans. The process to determine reliability critical units is a good start, but there are issues such as workable analysis protocols, interconnect concerns among states, regional transmission operators and power systems, and projecting plant closures and retrofit timelines

Although broad-based reliability studies have indicated that there may not be nationwide reliability issues, the grid is not nationwide. It is regionalized, with some regions having stronger systems and better interconnections than others. One major gap in work done to date is the lack of any analysis of interface or seams issues: regions, states and even individual companies now will have to pay far more attention to what is happening at their borders as well as focusing on what is happening within their borders. Planning decisions need to be made sooner than later to assure that the outages, retirements, replacement power and transmission connections are coordinated and orderly to minimize upward pressure on compliance costs and potential power shortages.

## CONCLUSION

States that benefit from coal for powering their economies have been engaged in debates about charting the course of their energy futures. The bill Senators Manchin and Coats are sponsoring regarding MATS and CSAPR, the judicial review of CSAPR, and the important analytical work of grid reliability experts all will contribute to safeguarding our citizens' health while they benefit from affordable, reliable electricity.

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